

Internal Revenue Service, Treasury

§ 1.1368-0

A advances S an additional \$1,000, which is not evidenced by a written instrument. There is no net increase under paragraph (c) of this section in year 2010.

(ii) The \$4,000 April repayment S makes to A and A's \$1,000 September advance are netted to result in a net repayment of \$3,000 for the taxable year on A's \$16,000 open account debt carried forward from 2009. Because there is no net increase in 2010, no basis of indebtedness is restored for the 2010 taxable year, and A realizes \$1,500 of income on the \$3,000 net repayment at the close of the 2010 taxable year.

(iii) At close of the 2010 taxable year, A's open account debt does not exceed \$25,000. The net repayment of \$3,000 for the taxable year on A's \$16,000 open account debt carried forward from 2009, leaves A with an open account debt of \$13,000 to carry forward as open account debt to the beginning of the 2011 taxable year.

Example 8. Treatment of shareholder indebtedness not evidenced by a written instrument which exceeds \$25,000. (i) The facts are the same as in *Example 7*, in addition to which, on February 1, 2011, S repays \$5,000 of the open account debt and on March 1, 2011, A advances S \$20,000, which is not evidenced by a written instrument.

(ii) At the close of the 2010 taxable year, A has an open account debt of \$13,000 to carry forward as open account debt to the beginning of the 2011 taxable year.

(iii) The 2011 advances and repayments are netted to result in a net advance of \$15,000 on A's \$13,000 open account debt carried forward from 2010, increasing A's open account debt to \$28,000 as of the close of the 2011 taxable year. Because A's open account debt exceeds \$25,000, for any subsequent taxable year the \$28,000 indebtedness will be treated in the same manner as indebtedness evidenced by a separate written instrument for the purposes of this section. Because there is no net increase in 2011, no basis of indebtedness is restored for the 2011 taxable year.

[T.D. 8508, 59 FR 16, Jan. 3, 1994, as amended by T.D. 9428, 73 FR 62202, Oct. 20, 2008; T.D. 9428, 73 FR 67389, Nov. 14, 2008; T.D. 9428, 73 FR 71545, Nov. 25, 2008]

§ 1.1367-3 Effective/Applicability date.

Section 1.1367-2(a), (c)(2), (d)(2), and (e) *Example 6*, *Example 7*, and *Example 8* apply to any shareholder advances to the S corporation made on or after October 20, 2008 and repayments on those advances by the S corporation. The rules that apply with respect to shareholder advances to the S corporation made before October 20, 2008, are contained in § 1.1367-3 in effect prior to October 20, 2008. (See 26 CFR part 1 re-

vised as of April 1, 2007.) Shareholders have the option to apply these rules to shareholder advances to the S corporation made before October 20, 2008, and repayments on those advances by the S corporation.

[T.D. 9428, 73 FR 62203, Oct. 20, 2008]

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§ 1.1368-3 Examples.

§ 1.1368-4 Effective date and transition rule.

[T.D. 8508, 59 FR 18, Jan. 3, 1994, as amended by T.D. 8696, 61 FR 67455, Dec. 23, 1996; T.D. 8852, 64 FR 71649, Dec. 22, 1999; T.D. 8869, 65 FR 3855, Jan. 25, 2000]

§ 1.1368-1 Distributions by S corporations.

(a) *In general.* This section provides rules for distributions made by an S corporation with respect to its stock which, but for section 1368(a) and this section, would be subject to section 301(c) and other rules of the Internal Revenue Code that characterize a distribution as a dividend.

(b) *Date distribution made.* For purposes of section 1368, a distribution is taken into account on the date the corporation makes the distribution, regardless of when the distribution is treated as received by the shareholder.

(c) *S corporation with no earnings and profits.* A distribution made by an S corporation that has no accumulated earnings and profits as of the end of the taxable year of the S corporation in which the distribution is made is treated in the manner provided in section 1368(b).

(d) *S corporation with earnings and profits—(1) General treatment of distribution.* Except as provided in paragraph

(d)(2) of this section, a distribution made with respect to its stock by an S corporation that has accumulated earnings and profits as of the end of the taxable year of the S corporation in which the distribution is made is treated in the manner provided in section 1368(c). See section 316 and § 1.316-2 for provisions relating to the allocation of earnings and profits among distributions.

(2) *Previously taxed income.* This paragraph (d)(2) applies to distributions by a corporation that has both accumulated earnings and profits and previously taxed income (within the meaning of section 1375(d)(2), as in effect prior to its amendment by the Subchapter S Revision Act of 1982, and the regulations thereunder) with respect to one or more shareholders. In the case of such a distribution, that portion remaining after the application of section 1368(c)(1) (relating to distributions from the accumulated adjustments account (AAA) as defined in § 1.1368-2(a)) is treated in the manner provided in section 1368(b) (relating to S corporations without earnings and profits) to the extent that portion is a distribution of money and does not exceed the shareholder's net share immediately before the distribution of the corporation's previously taxed income. The AAA and the earnings and profits of the corporation are not decreased by that portion of the distribution. Any distribution remaining after the application of this paragraph (d)(2) is treated in the manner provided in section 1368(c) (2) and (3).

(e) *Certain adjustments taken into account—(1) Taxable years beginning before January 1, 1997.* For any taxable year of the corporation beginning before January 1, 1997, paragraphs (c) and (d) of this section are applied only after taking into account—

(i) The adjustments to the basis of the shares of a shareholder's stock described in section 1367 (without regard to section 1367(a)(2)(A) (relating to decreases attributable to distributions not includible in income)) for the S corporation's taxable year; and

(ii) The adjustments to the AAA required by section 1368(e)(1)(A) (but without regard to the adjustments for